

PASS-THROUGHS: THE UNKNOWN ENTITIES

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PASS-THROUGHS: THE UNKNOWN ENTITIES

I. BUSINESS CONSIDERATIONS

- A. Term of Existence.
- B. Transferability/Pledgeability of Ownership Interests.
- C. Limitation of Liability.
 - 1. Limited partnership must have at least one general partner, and Limited Partners cannot participate in management of business.
 - 2. All members of LLC and all shareholders in a corporation have limited liability and can participate in management.
- D. Expense and Complexity of Formation and Operation.
 - 1. State filing fees.
 - 2. Comparison of IRC §§721 and 351.
 - 3. Necessity of board meetings, shareholder meetings and other governance issues.
 - 4. Fiduciary duties.
- E. Raising Capital.

II. CONSIDERATIONS/WHO IS TAXED

- A. Double taxation of C corporation income.
- B. Applicable Rate.
 - 1. Corporate.
 - 2. Individual.
- C. Special allocations of income and deductions.
- D. Tax accounting rules/cash/accrual.

- E. Choice of taxable year.
 - 1. Availability of deferral.
 - 2. Required and permitted years.
- F. Loss limitation rules.
 - 1. Net operating loss carryback/carryover.
 - 2. Basis limitations.
 - 3. At risk limitations.
- G. Alternate minimum tax.
- H. Estimated tax payments.
- I. Return filing requirements.
 - 1. Entity returns.
 - 2. Owner returns.

III. THE PROLIFERATION OF PASS-THROUGH ENTITIES.

- A. The Tax Reform Act of 1986.
 - 1. Repeal of the General Utilities doctrine.
 - a. Significantly increased the incidence of double taxation upon C corporations, e.g., repeal of IRC §337.
 - b. Made individual marginal tax rate lower than corporate for first time in decades.
 - 2. Liberalization of S corporation rules.
 - a. Increase to 75 shareholders.
 - b. Certain trusts permitted as shareholders.
 - c. Non-voting stock permitted.

- d. Passive income permitted (if not a former C corporation).
- 3. But still significant limits on S corporations.
 - a. No accumulation trust/sprinkle trust permitted (now permitted beginning in 1998).
 - b. No 501(c)(3) or ESOP shareholders permitted (now permitted beginning in 1998).
 - c. No subsidiaries permitted (now permitted beginning in 1998).
 - d. Only one class of stock permitted (except voting rights).
 - e. Built-in gains tax.
- B. New Entity Classification Regulations ("Check-the-Box").
 - 1. Prior rules to achieve partnership (pass-through) status were onerous and difficult to apply.
 - a. Associates.
 - b. An objective to carry on the profits and divide the gains therefrom.
 - c. Continuity of life.
 - d. Centralization of management.
 - e. Liability for corporate debts limited to corporate property.
 - f. Free transferability of interests.
 - 2. New classification "check-the-box" regulations adopted by Treasury effective January 1, 1997. Treas. Reg. §§301.7701-1 through -3.
 - a. Unincorporated organizations (under state law) are taxed as partnerships (default status), but can elect to be taxed as a corporation (could be C corp. or S corp.) regardless of their seeming preponderance of corporate characteristics under the old regulations. Thus, an LLC is taxed as a partnership unless it elects not to do so. Exception: A single-member LLC cannot be a partnership because a partnership must have at least two partners. Thus, the regulations provide that a single-member

LLC is a "disregarded entity" (default) but can elect to be taxed as a corporation.

- b. An organization that is a corporation under state law is a corporation for federal income tax purposes.

IV. THE "BEAUTY" OF THE LIMITED LIABILITY COMPANY

- A. The first LLC statute was enacted in Wyoming in 1977. All 50 states and the District of Columbia now have LLC statutes, although they are not uniform.
- B. Fundamental advantage of LLC: limited liability for all members combined with pass-through tax treatment.
- C. Advantages of LLC over S corporation.
 - 1. S corporations are not permitted to have more than 75 shareholders; there is no limitation upon the number of members which an LLC can have provided, however, that an LLC whose membership interests are publicly traded will, with very limited exceptions, be treated as a C corporation. There are a great many business organizations having more than 75 shareholders but which are not publicly traded.
 - 2. Certain types of taxpayers are prohibited from being S corporation shareholders (such as C corporations and nonresident aliens). No such limitations exist with respect to LLC membership. An S corporation is permitted to have only one class of stock (except that it can have classes which differ only as to voting rights). An LLC can have multiple classes of membership and have any type of special allocation of income or deduction permitted under the partnership tax rules.
 - 3. Like a partnership, an LLC member's proportionate share of indebtedness of the LLC is included in the member's basis in the LLC. This is important in determining the amount of loss from the entity which the member might be able to deduct on his or her personal tax return. Debt of an S corporation gives no basis to the S corporation shareholder, even if such debt is personally guaranteed by the shareholder. The shareholder's basis in his interest in the S corporation is limited to his basis in his stock and any loans personally made to the corporation.
 - 4. Contributions of property to an LLC in exchange for a membership interest in the LLC are governed by IRC §721 which generally

provides that the contribution is tax free. A similar contribution made to a corporation (whether C or S) is governed by IRC §351 which affords tax-free treatment only if the transferor of the property has at least 80% control of the corporation immediately after the transfer or is a member of a group of transferors making transfers and the group has such control.

5. Distributions of appreciated assets from an S corporation to a shareholder trigger gain recognition at the corporate level. An LLC, under the partnership rules, generally realizes no gain on appreciated property distributions to partners.

V. WHY ARE THERE STILL S CORPORATIONS?

- A. Existing S corporations cannot convert to LLC status tax free. Such conversion is a taxable liquidation of the S corporation.
- B. Distributive share of S corporation income is not subject to self-employment and medicare taxes (LLC/Partnership distributive shares generally are subject to these taxes).
- C. S corporations can issue incentive (qualified) stock options (must be "stock" so LLC cannot do this).
- D. Client and attorney familiarity with the corporate form, including well-developed case law on fiduciary duties of officers and directors.
- E. Some state laws require that certain types of businesses (e.g., banks, public utilities) be conducted by a "corporation".

VI. WHAT ABOUT THE C CORPORATION?

- A. An entity whose ownership interests are publicly traded generally cannot achieve pass-through tax status (narrow/limited exceptions such as REITs).
 1. An S corporation is limited to 75 shareholders.
 2. With narrow exceptions, a "publicly traded partnership" (including LLC) is taxed as a C corporation. IRC §7704(a).
- B. There are still a few employee benefit advantages to C corporation owner/employees not available to owner/employees of pass-throughs (e.g.,

fully deductible health insurance, group life insurance). However, pension, profit-sharing and 401(k) rules are now generally the same for all entities.

- C. Some taxpayers strategize: pay out most of the income to the owners as salary, leave enough in the corporation to take advantage of the 15% tax bracket.
- D. Many closely-held C corporations "stuck" there.
 - 1. Conversion to LLC is taxable liquidation.
 - 2. Cannot elect S status because:
 - a. Have ineligible or too many shareholders.
 - b. Election triggers recognition of LIFO reserve.
 - c. Concern about future exposure to built-in gains tax.

VII. STATE TAXATION OF PASS-THROUGH ENTITIES

- A. Lack of uniformity of state taxing schemes applicable to pass-throughs is a barrier to taxpayer compliance and, therefore, to state revenue collection.
- B. As a very general rule, it can be said that a substantial majority of the states having income taxes apply the federal pass-through scheme; i.e., no entity tax, tax imposed upon owners.
 - 1. A number of states which recognize pass-throughs do not treat S corporations, LLCs, and partnerships in identical fashion.
 - 2. A number of states impose "fees" upon pass-throughs at the entity level, e.g., New York, California.
 - 3. Many states apply a privilege or franchise tax but recognize pass-through of the income, e.g., Kentucky. In some states these taxes apply to S corporations because they are corporations, but not to LLCs and partnerships (planning opportunity for taxpayers).
 - 4. Some states require that pass-throughs file returns, others do not. In some states a return is required only if there are nonresident owners, otherwise not.

C. The nature of the pass-through multiplies the challenge of tax compliance, collection.

1. In general, individual taxpayers are subject to state income tax on:

- a. 100% of their share of pass-through income in their state of residence, plus
- b. their share of income apportioned to each other state in which the entity had nexus.

Example: S corporation X has two equal shareholders, shareholder O lives in Ohio and shareholder K lives in Kentucky. X has total taxable income for year of 1M of which \$300K was apportioned to Ohio, \$300K was apportioned to Kentucky, and \$600K was apportioned to Illinois. Shareholder O includes \$500K (50% shareholder) in his Ohio return, and must also file nonresident returns in Kentucky and Illinois, paying tax on his 50% of the income apportioned to those states. Shareholder K pays tax on \$500K in Kentucky and files nonresident returns in Ohio and Illinois. Further, the corporation must pay the Kentucky Corporation License Tax (a net worth tax) and pay the Illinois "personal property replacement tax" on 1 1/2% of its net income.

- c. the shareholders must rely upon the imperfect system of tax credits in their home state to avoid double taxation. Should they receive a credit for the Illinois entity-level tax?

2. Compounding factors.

- a. What if, in the above example there were 25 shareholders living in 10 states and the corporation had nexus in 20 states?
- b. In each of the states in the above example, there are differing state modifications to taxable income.
- c. Each of the three states has a different apportionment formula.
- d. Ohio requires withholding on the nonresident's distributive share, Kentucky and Illinois do not.

D. Nonresident Corporate Limited Partners/Members.

1. Generally, states believe that they have jurisdiction to tax a corporation whose only activity in the state is as a limited partner in a partnership or member of an LLC where the entity is doing business in the state. People ex rel. Badische Anlin Soda Fabrik v. Roberts, 42 N.Y.S. 502 (1896) (German corporation, whose only tie to New York was ownership of a limited partnership interest in a New York partnership was subject to New York tax). However, some states will not assert taxing jurisdiction if the entity activity is passive investment only, not the conduct of a trade or business. See, e.g., Virginia Dept. of Taxation P.D. 95-280 (Nov. 3, 1995).
2. How is the distributive share of income of the pass-through taxed in the hands of its corporate corporation?
 - a. It must be determined whether the pass-through entity's income is business income or nonbusiness income. Some states make this determination at the pass-through entity level while others make this determination at the C corporation level.
 - b. California requires that if income from the pass-through constitutes business income, the corporation must determine whether or not the corporation and the pass-through are engaged in a single unitary business. If they are so engaged, the pass-through entity income must be combined and apportioned with the corporation's other business income. If not, the items are treated as arising in the separate trade or business of the corporation and must be apportioned separately from the corporation's other business income. The C corp.'s distributive share of business income is aggregated with its other income, without eliminating sales between the C corp. and the pass-through entity.
 - c. Illinois requires a C corp. partner/member to include in its Illinois income as much of the pass-through entity's business income as is allocated or apportioned to the state in the hands of the pass-through entity. Illinois' partnership regulations provide that a partnership's business income is combined and apportioned with the corporate partner's business income if the partnership and the partner are unitary.
 - d. If a C corporation and the pass-through entity are unitary, the C corporation generally combines its distributive share of the pass-through entity's income and apportionment factors with

its operating activities. It is not clear how the share of factors is determined. Most states provide that a corporate partner's factors are determined as the same percentage of income or of loss.

- e. Some states provide that inter-company sales between the corporation and the pass-through entity are eliminated from both the numerator and denominator of the corporation's sales factor to the extent of the corporation's interest in the partnership.

E. Enforcement Mechanisms.

- 1. Composite returns.
- 2. Withholding requirements.

VIII. DISREGARDED ENTITIES

A. Types of disregarded entities.

- 1. Single-member limited liability companies. Under the check-the-box regulations a single-member LLC is a disregarded entity unless it affirmatively elects to be taxed as a corporation. Treas. Reg. §301.7701-2(a) & (b).
- 2. Qualified subchapter S subsidiaries are disregarded entities and have been permitted by statute since 1997. A corporate subsidiary of an S corporation cannot qualify for QSSS treatment unless wholly owned by the S corporation. IRC §1361(b)(3).
- 3. Qualified REIT subsidiaries have been permitted as disregarded entities since 1986.

B. Selected income tax issues regarding disregarded entities.

- 1. Does the presence of a disregarded entity in a state create nexus for the owner of the entity in that state where the owner has no other contact with the state?
- 2. Can the disregarded entity claim the protection of P.L. 86-272 on its own?

3. Should the income of the disregarded entity be characterized as business or nonbusiness on a separate basis?
 4. Combined apportionment.
 5. The growing use of single-member LLCs as corporate subsidiaries in order to avoid the federal consolidated return regulations.
- C. Are disregarded entities to be disregarded for purposes of other taxes such as sales and use tax and real estate transfer taxes?

SPONSOR TESTIMONY

NOTE: RED wording incorporates House amendments that were **ADDED** to HB143.
BLUE wording incorporates House amendments that **DELETED** sections of HB143.

This bill deals with clarifying the income taxation of “pass through entities” such as S corporations, partnerships, and limited liability companies. A “pass through entity” is not taxed at the entity level but the tax is imposed upon each shareholder, partner, manager, or member’s share of the entity’s income on their individual income tax return.

In addition, this bill

- Defines more clearly “Montana Source Income” for residents and non-residents as used within the Multistate Tax Compact found in 15-1-601.
- provides for one of three methods for an entity, or participant to file a return and pay any tax due. These three methods are:
 1. a composite, or combined return is filed by the entity and the entity pays the tax on behalf of all participating non-resident shareholders, partners, managers, or members.
 2. a Consent Agreement is signed by a non-resident agreeing to file a Montana individual income tax return and pay any tax due timely, or;

3. an entity is required to withhold and remit an estimated tax from a nonresident's share of Montana source income reported on the entities information return ~~the distributive share of the income earned by each nonresident.~~

- temporarily requires the department to give notice to entities informing them of the requirements to file a composite return or a non-resident consent agreement or remit and estimated tax on those non-residents who do not participate with the other two methods.
- allows residents a tax credit against their individual income tax liability for taxes imposed and paid at the S-Corporation, or Small Business Corporation level to another state or country.
- provides a penalty for failure to file an information return such as an S corporation or partnership return with the state.
- requires the secretary of state to report on newly established pass-through entities to the department of revenue by December 31st of each year.
- ~~• creates an interim committee to conduct a study on the reporting and taxation of income that flows through pass-through entities.~~
- Provides for the department to review and make recommendations to the revenue and taxation interim committee, the reporting and taxation of income that flows through pass-through entities.

This bill is being introduced because:

- Pass-through entities are becoming more popular and have steadily increased the past five years. Montana and multi-state businesses are increasingly conducting business through small business corporations, partnerships and other alternative entities such as limited liability companies (LLC) and limited liability partnerships. (LLP).
- Federal information indicates that the growth of S-Corporations has increased by 28% from 1997 to 1998.
- State information indicates that S-Corporation growth has increased at the rate of 10% per year.
- State information indicates that the conversion of C-corporations to S-Corporations was up 17% from 1998 to 1999.
- Department of revenue records show 8,306 partnership returns were filed in 1994 and 10,389 partnership returns were filed in 1998. This is an increase of 25%.
- The Secretary of State reported approximately 5,500 Limited Liability Companies registered in 1999.
- Partnership and Subchapter S corporation tax return information that must be submitted to the department of revenue is limited, and compliance with Montana tax laws by non-residents is lacking. A recent compliance project conducted by the department of revenue resulted in additional revenues of \$634,392 from non-resident S-Corporation shareholders and \$214,964 from non-resident partners in partnerships for not filing a Montana individual income tax return.

By revising the income taxation of these "pass-through entities", defining the various types of pass-through entities, and requiring these entities to file a composite return, withhold from distributive shares, or require a shareholder to file a consent form, the tax gap created by non-voluntary compliance by non-residents will be reduced.

Mr. Chairman and Committee Members, I hope you will give this bill your full consideration and recommend a DO PASS.

SHORT BILL DESCRIPTION

The purpose of this legislation is to clarify the Income Taxation of "pass-through entities" defined as:

- S corporations
- Partnerships
- Limited Liability Companies and
- other pass-through entity income.

This legislation further provides for:

- an entity to file a composite return and pay the tax on behalf of all non-resident shareholder, partners, members, or managers;
- a non-resident shareholder, partner, member or manager to file a Montana consent agreement, agreeing they will be subject to Montana law and file a return;
- an entity to do withholding from non-residents of a portion of their distributive share of income and remit this backup withholding to the state of Montana in accordance with MCA 15-30-142;
- a penalty to be assessed against a pass-through entity for failure to file a return;
- a resident shareholder to take a credit against their individual income tax liability for taxes imposed on an S-Corporation by another state or country; and
- ~~the creation of an interim committee to conduct a study of the reporting and taxation of income that flows through pass-through entities.~~
- the department to review and make recommendations to the revenue and taxation interim committee, the reporting and taxation of income that flows through pass-through entities.

LONG BILL DESCRIPTION

This bill deals with clarifying the income taxation of "pass through entities" such as S corporations, partnerships, limited liability companies, and other pass-through entity income. A "pass through entity" is not taxed at the entity level but the tax is imposed upon each shareholder, partner, manager, or member's share of income at the individual income tax level.

In addition, this bill defines "Montana Source Income" for residents and non-residents. For a resident "Montana Source Income" is all income earned in-state and out-of-state by an individual whether they earn it directly as an individual or receive it through a pass-through entity. For non-residents "Montana Source Income" is defined as income earned for actual service performed within the state or from income received from the connection with a trade, business, or occupation carried on in this state whether this is in a self-employed business or income received through a pass-through entity.

The bill further provides for an entity to elect to file a composite return and make composite payments of tax on behalf of all of its non-resident shareholders, partners, managers, or members. Or, the non-resident shareholder, partner, manager, or member may file a Montana Consent Agreement stating they agree to be subject to Montana law and file a return. In the absence of filing a composite return or a consent agreement the entity is required to withhold a tax from their distributive share of the income. The bill provides for a temporary section that requires the department to give notice to entities of these requirements through December 31, 2002. The permanent section does not require the department to give notice and is effective for tax years beginning after December 31, 2002.

This bill further allows a resident of Montana a tax credit against their individual tax liability imposed by Title 15 Chapter 30, which is the "Individual Income Tax" statute, for taxes imposed on an S-Corporation by another state or country.

This bill also provides for a penalty to be assessed against the pass-through entity for failure to file an information return. This penalty would be applied using the uniform penalty statute located in MCA 15-1-216 except the amount of the penalty would not be based on the amount of tax due but at a rate of ~~\$50.00~~ \$10.00 per month up to 5 months times the number of partners, shareholders, managers, members or other owners. This penalty does not apply to an entity with 10 or fewer partners, shareholders, managers, or members who have filed their individual return or report and paid all taxes due.

In addition, this bill requires the Secretary of State to report, in addition to corporations, limited partnerships, limited liability companies, and limited liability partnerships to be reported by to the department of revenue on or before December 31st of each year.

~~This bill also establishes a pass through entity committee of eight individuals representing the legislature, business, accountants and the executive branch.~~ This bill provides for the department, along with interested parties, ~~committee is~~ directed to study the reporting and taxation of income that flows through pass through entities, the pass through entities method of reporting, and other state practices. The review ~~committee~~ is to consider recommendations to ensure equitable treatment of these entities. The department is to report to the revenue and taxation interim committee at least once a year their findings and recommendations.

BENEFITS/ISSUES

Pass-through entities are becoming more popular with recent changes in federal statute and have steadily increased the past five years. Montana and multi-state businesses are increasingly conducting business operations through partnerships and other alternative entities such as limited liability companies' (LLC) and limited liability partnership (LLP).

Benefits of this legislation include:

- Provides a clear definition of "Montana Source Income" moving Montana forward in preparation for the increased popularity of pass-through entities.
- Makes provisions for a pass-through entity to file a composite return and pay any individual income tax liability on behalf of the non-resident participants.
- Provides for a non-resident to sign an agreement with the department that they will file a Montana individual income tax return in compliance with Montana statute.
- Requires a back-up withholding or estimated payments by the entity on non-resident who do not participate in a composite return or sign a consent agreement. (Provides for an interim period in which the department must give notice to entities of their filing and reporting requirements.)
- Increases voluntary compliance efforts by non-residents by providing for composite returns, back-up withholding, or a consent agreement that a non-resident will file a Montana tax return and comply with the states income tax laws.
- Requires the entity to supply the department with a copy of their federal return.

- Establishes a penalty for failure to file an information return by a pass-through entity.
- Identifies Limited Liability Companies and Limited Liability Partnerships as entities along with partnerships and S corporations to file information returns.
- ~~• Establishes an interim committee to study the reporting and taxation of income as it flows through an entity to the individual and taxed at the individual income tax level, and provide for a recommendation on how the state should ensure fair and equitable taxation of income.~~
- Provides for the department to review and make recommendations to the revenue and taxation interim committee, the reporting and taxation of income that flows through pass-through entities.

IMPACTS

- Increases voluntary compliance by providing in statute a definition of “Montana Source Income”, requiring back-up withholding on non-residents, composite returns to be filed, or an agreement that a non-resident will file a return with Montana.
- Increases tax payments as evidenced by a recent compliance project conducted by the department of revenue. This pilot project resulted in additional revenues of \$634,392 from non-resident S-Corporation shareholders and \$214,964 from non-resident partners in partnerships for not filing a Montana individual income tax return.
- ~~Establishes an interim committee to study the taxation of pass through entities.~~
- Requires to department to review and make recommendations, with the assistance of interested parties, on the reporting and taxation of income that flows through pass-through entities.
- The department will provide their findings and recommendations to the revenue and taxation interim committee at least once a year.

SECTION BY SECTION

Section 1: Limitations on contributions from political committees.

- Amends 13-37-218 to eliminate the sub-paragraph reference for the definition of “inflation factor” found in 15-30-101.
- This is a house keeping change only. This eliminates all references to sub-paragraphs and makes reference by sections only. As further legislation adds or deletes definitions this reduces the need to amend sections that make reference to specific paragraph numbers.

Section 2: Definitions

- Adds to section 15-30-101 new definitions for terms used in this bill. These new terms include:
 - **“CORPORATION OR C CORPORATION”**
 - Definition #3
 - a separate entity for federal tax purposes
 - is not a Sub S corporation (Small Business Corporation) for federal tax purposes.
 - **“DISREGARDED ENTITY”**
 - Definition #5
 - An entity that is disregarded separately from its owner whereas a business entity is an entity separately recognized for federal tax purposes.
 - Is treated in the same manner as a sole proprietorship, branch, or division of the owner.
 - A business entity that is not classified as a corporation can elect its classification for federal tax purposes under the “check the box” regulation and filing Federal Form 8832 “Entity Classification Election.”
 - **“DIVIDENDS”** Adds to the existing definition;
 - Definition #6
 - Distributions made by an S-Corporation treated as dividends for federal tax purposes are also dividends for Montana purposes.

- **“INTERNAL REVENUE CODE”**
 - Definition #12
 - Defines the Code as the Internal Revenue Code (I.R.C.) of 1986, or as subsequently written as a result of federal changes.
 - As federal legislation changes and the I.R.C. changes Montana adopts these changes unless specifically addressed in Montana statute.
- **“LIMITED LIABILITY COMPANY”**
 - Definition #14
 - Makes reference to the Montana Limited Liability Company Act found in Title 38, Chapter 8.
- **“LIMITED LIABILITY PARTNERSHIP”**
 - Definition #15
 - Makes reference to the Limited Liability Partnership definition found in Title 36, Chapter 10.
- **“MONTANA SOURCE INCOME”**
 - Definition #17
 - Spells out in more detail the Multistate Tax Compact, which is found in MCA §15-1-601. The purpose of this statute is to:
 - Facilitate proper determination of state and local tax liability
 - Promote uniformity
 - Facilitate taxpayer convenience and compliance
 - Avoid duplicative taxation.
 - **for residents** include all: (no matter what state or country it was earned, received or accrued in)
 - i. wages, salary, tips and other compensation;
 - ii. gains from the sale or transfer of tangible property;
 - iii. gains from the sale or transfer of intangible property;
 - iv. interest;
 - v. dividends;
 - vi. business net income or losses;
 - vii. farming activity net income or losses;
 - viii. net rent proceeds;
 - ix. net royalties;

- x. patent royalties;
- xi. net copyright royalties;
- xii. partnership income, gain, loss, deduction or credit;
- xiii. S Corporation income, gain, loss, deduction or credit;
- ~~xiv. estate or trust income, gain, loss, deduction or credit;~~
- xiv. social security benefits;
- xv. taxable retirement income;
- xvi. any other income.
- **for non residents** include:
 - the 4716 items listed above but is limited to:
 - income earned, received or accrued for work performed in Montana, or;
 - income derived from or connected with a trade, business, or occupation carried on Montana.
 - Income from the sale of Montana property.
- **“NONRESIDENT”**
 - Definition #19
 - any individual who is not considered a resident of Montana.
- **“PARTNER”**
 - Definition #21
 - if treated as a partner for federal tax purposes then they are a partner for Montana tax purposes.
- **“PARTNERSHIP”**
 - Definition #22
 - if treated as a partnership for federal purposes then they are a partnership for Montana tax purposes.
- **“PASS-THROUGH ENTITY”**
 - Definition #23
 - An entity, whose income or loss is passed through to the shareholder, partners manager or member and taxed on their individual income tax return.
 - an entity that does not pay any tax, but is required to file an information return.
 - An entity whose existence is disregarded for federal income tax purposes, or in other words: (a limited liability companies not recognized for

federal tax purposes as an entity. This type of entity elected for federal purposes to be treated as a C-Corporation, an S-Corporation, a Partnership, or a sole proprietor and files accordingly).

- **“S CORPORATION”**

- Definition #28
- Same as a small business corporation and who is has elected for federal tax purposes to be treated as a small business corporation and have their income or loss pass through to their individual income tax return.

Section 3: Taxation of partners, shareholders, members and managers

- **NOTE: Residents** of Montana include in there Montana source income **all** income no matter what state it is earned in.
- **Non-residents** include in their Montana source income **only** that income earned **within** the state of Montana.
- Residents and non-residents of a pass through entity such as a:
 - Partner of a partnership;
 - Shareholder of an S Corporation (Small Business Corporation); or
 - Partner, shareholder, manager, or member of a limited liability company or limited liability partnership
 - who has “Montana Source Income” must include their net income on their individual income tax return their share of income, gain, loss, deductions and credits received from the pass-through entity.
- Must provide a copy of their federal schedule (K1) “Shareholder’s or Partners Share of Income, Credits, Deductions, etc.”

Section 4: Composite (or combined) tax return and payment of tax by the entity on behalf of the nonresidents

- A combined individual income tax return (in lieu of each individual return) may be filed by a pass-through entity on behalf of the nonresident shareholders, partners, and members and their respective individual income tax liability paid by the entity on behalf of the individuals. (Residents cannot file this way).

- In order for a non-resident to be included on the combined return their "Montana Source Income" must only come from a pass-through entity. They do not qualify to file a combined return if they have "Montana Source Income" from other activities.
- Each participating nonresident is entitled to the standard deduction and one exemption.
- Each participating non-resident is taxed on their taxable income using the appropriate tax rates of 2% to 11%.
- The total amount of tax liability for each participating individual is combined and paid by the entity on behalf of each nonresident.
- The entity electing to file a composite (combined) return must make quarterly estimated tax payments computed separately for each participant at: ~~of:~~
 - 90% of the current years ~~combined~~ tax liability, or;
 - 100% of the prior years ~~combined~~ tax liability, and;
 - their combined tax liability is \$500 or more after credit of any withholding or estimated payments made.

Section 5: A nonresident consent agreement or withholding requirement Temporary statute effective October 1, 2001 for tax years beginning after December 31, 2001 and terminates December 31, 2002.

- **This section requires the Department to give NOTICE** to each entity of the need to either comply with filing a composite return or file a nonresident consent agreement.
- Entity has the later of 180 days after the due date of an information return or after receiving notice from the Department to remit the estimated (withheld) tax from non-participating non-residents.
- If the department does not send notice then the entity is not subject to withholding.
- In lieu of filing a composite return, a nonresident shareholder, manager, member or partner may file a consent agreement with Montana stating they agree to be subject to Montana income tax laws and file an individual income tax return.
- In lieu of filing a composite return by the pass-through entity or filing the consent agreement the pass-through entity is required to withhold a tax on nonresident shareholders, managers, members or partners based on their distributive shares of Montana source income.

- Amount withheld by the entity is the highest marginal tax rate in effect under 15-30-103. Currently this rate is 11%)
- Any amount withheld and paid by the entity is considered payment by the nonresident individual and credit to their return when their return is filed.
- The entity is entitled to recover any payments made on behalf of a nonresident partner, shareholder, manager or member.

Section 6: A nonresident consent agreement or withholding requirement.

- **Permanent statute** that will be codified as the same code section number as the temporary section 5 listed above.
- This section is effective January 1, 2003 and applied to tax years beginning after December 31, 2002.

Section 6: ~~Credit allowed individual resident shareholder for income taxes imposed and paid by an S corporation (Small Business Corporation) to another state or country.~~ This section is eliminated and the contents included in Section 8, which is amending MCA 15-30-124 "Credit allowed resident taxpayers for income taxes imposed by foreign states or countries."

- ~~• Residents of Montana are allowed a credit against their individual income tax liability for the pro rata share of income taxes imposed and paid to another state or country by an S corporation.~~
- ~~If another state or country assesses an income tax against a pass through entity such as an S Corporation it is considered a tax assessed and paid by the individual shareholder. Therefore, the resident shareholder is entitled to a credit for taxes paid to another state or country based on their share of the entity.~~

Section 7: Individual income tax on Nonresidents

- Adds to the existing statute 15-30-105 a clarification that no income, gain, loss, deduction, expense or credit may be counted more than once in determining Montana source income.

Section 8: Credit allowed individual resident shareholder for income taxes imposed and paid by an S corporation (Small Business Corporation) to another state or country.

- Adopts language from SB2. This section is effective on passage and approval.
- Applies retroactively to tax years beginning after December 31, 2000. (NOTE: SB2 IS RETROACTIVE TO TAX YEARS BEGINNING AFTER DECEMBER 31, 1996.)
- Residents of Montana are allowed a credit against their individual income tax liability for the pro rata share of income taxes imposed and paid to another state or country by an S corporation.
- If another state or country assesses an income tax against a pass through entity such as an S Corporation it is considered a tax assessed and paid by the individual shareholder. Therefor, the resident shareholder is entitled to a credit for taxes paid to another state or country based on their share of the entity.

Section 8-9: Income or License taxes involving pass through entities—information returns required.

- Partnerships, S corporations, and other pass through entities are not subject to taxes imposed in Title 15 chapter 30 (Individual Income Tax) or 31 (Corporate License Tax).
- An information return is required to be filed with the department of revenue and must include a copy of their federal return. (Form 1065 –Federal Partnership return, and Form 1120S –Federal Small Business Corporation return.)
- Bad debt reserve income realized for federal income tax purposes by financial institutions that elect to be treated as a Subchapter S Corporation is not taxable if it exceeds the deduction allowed in 15-31-114.
- A penalty of ~~\$50~~ \$10 per month for a maximum of 5 months times the number of partners, shareholders, managers, or other owners is assessed for late filing of a Montana information return.
- The department may waive the penalty for reasonable cause as provided in §15-1-206.
- The \$10 penalty does not apply if the pass through entity has 10 or fewer partners, shareholders, managers, members or other owners whom have filed an individual income tax return and have paid all taxes when due.

Section 9-10: Estimated tax – payment – exceptions – interest.

- Amends 15-30-241 to eliminate the sub-paragraph reference for the definition of “gross income” found in 15-30-101.
- This is a house keeping change only. This eliminates all references to sub-paragraphs and makes reference by sections only. As further legislation adds or deletes definitions this reduces the need to amend sections that make reference to specific paragraph numbers.

Section 40 11: Organizations subject to corporate license tax

- Amending 15-31-101, MCA to include in the term “corporation”
 - limited liability company;
 - limited liability partnership;
 - partnerships; or
 - other entities that are recognized for federal income tax purposes as a separate entity.

Section 44 12: Qualifications to be eligible for a tax credit for contribution to qualified endowment.

- Adds to 15-31-162, MCA the wording that an entity must ~~be engaged in a trade or business~~ carry on a trade or business for which deductions are allowed under IRC §162 (trade or business expenses) to qualify for the qualified endowment credit.

Section 42 13: Definition of “small business corporation”

- Adds to 15-31-201, MCA (Corporation license tax statutes) that a small business corporation is synonymous with the term “S Corporation” defined in the individual income tax statutes (Title 15, Chapter 30).
- References the Internal Revenue Code section 1362, which is the federal statute recognizing small business corporation status.

Section 43 14: List of entities furnished by secretary of State of Montana

- Requires the Secretary of State to include limited partnerships, limited liability companies, and limited liability partnerships to be reported annually to the Department of Revenue.

~~Section 14: Pass through entity committee membership purpose~~ Replace with new Section 15.

- ~~• Creates an interim committee composed of 8 members including:~~
 - ~~• 2 members from the house (both parties)~~
 - ~~• 2 members from the senate (both parties)~~
 - ~~• 1 member representing small business~~
 - ~~• 1 member representing larger businesses~~
 - ~~• 1 member representing accountants~~
 - ~~• 1 member from the executive branch~~

Section 15: Review of pass-through entity taxation by the department.

- The department will study and review the reporting and taxation of pass-through entities with the assistance of interested parties (Montana Society of CPA, Montana Taxpayer's Assoc., etc.)
- Make recommendations that ensure fair and equitable taxation of pass-through entities income as it flow through one entity to another.
- Will report to the revenue and taxation committee at least once a year their findings and recommendations.

~~Section 16:~~ Codification instruction

~~Section 17:~~ Repeals Corporate License tax sections:

- 15-31-202, MCA.
 - A small business corporation is not subject to the Montana corporation license tax but the shareholder must include their distributive share in their adjusted gross income per the individual income tax statutes. (Title 30, chapter 30).
 - This section is being replaced with the terminology found in Section 3 of this bill.
- 15-31-209, MCA.
 - If a corporation does not qualify for the federal small business classification (Sub S Corporation classification) or election the department may revoke their small business corporation status with the state.
 - This section is being replaced with the terminology found in Section 2 of this bill that defines S Corporations.

Section 18: Effective Dates

- Effective October 1, 2001 (except for)
 - **Section 8:** effective on passage and approval. (Credit allowed individual residents for S-corporation taxes paid to another state.)
 - **Section 6:** effective January 1, 2003 (Permanent statute on consent or withholding.)

Section 17-19: Applicability

- Applies to tax years beginning after December 31, 2001(except for)
 - **Section 8:** applies retroactively to tax years beginning after December 31, 2000. (Credit allowed individual residents for S-Corporation taxes paid to another state.)
 - **Section 6:** applies to tax years beginning after December 31, 2002. (Permanent statute on consent or withholding.)

Section 20: Termination

- **Section 5:** terminates December 31, 2002 (Temporary statute on consent or withholding)

INTERESTED PARTIES

Montana Society of Certified Public Accountants

- A tax bill that affects filing and reporting requirements for pass through entities along with individuals. May have impact on accounts since the bill requires such items as:
 - Withholding or estimated payments for nonresidents
 - composite return may be filed for nonresidents
 - consent agreement may be required.
- May have some opposition from the CPA society, as it does require more paperwork and they have concerns about the composite return.

Montana Taxpayer Association

- A tax bill that affects filing and reporting requirements for pass through entities along with individual.
- Should have limited affect on resident taxpayers as the bill primarily addresses requirements for nonresident
- Does provide a credit for taxes paid at the S-corporation level for resident taxpayers.
- Does require an information return to be filed by the entity with provision for penalties if no return is filed.
- Should have the support of the Montana Taxpayer Association.

Secretary of State

- Requires the Secretary of State to report annually to the department of revenue in addition to corporations, limited partnerships, limited liability companies and limited liability partnerships.
- Should have the support of the Secretary of States office.

Montana Small and Large Businesses

- Should have limited affect on Montana business that has no nonresident shareholders, partners, members or managers.
- May require additional bookkeeping and reporting if the Montana business has non-resident shareholders, partners, members or managers.
- Does require an information return to be filed by the entity with provision for penalties if no return is filed.
- Should have the support of this taxpayer group.

Multi State and/or other State Business

- Since this bill deals primarily with nonresident filing and reporting requirements this group may have the largest number of interested persons. Historically this group has numerous non-resident partners, shareholders, members or managers who are not familiar with Montana tax statutes and is the group where most non-filers exist.
- Would be the largest group filing composite (combined returns).
- This bill adopts various sections from other state statutes so the requirements should not be new to all out of state or multi state businesses.
- Will have some opposition by this group to complying with more procedures. However, for some it will also be a time and perhaps money saver to be able to deal with the Montana return without an individual involvement.

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TITLE 15. TAXATION CHAPTER 30. INDIVIDUAL INCOME TAX

Part 11. Pass-Through Entities

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15-30-1101. Definition of "small business corporation". (1) Except as provided in subsection (2), the term "small business corporation" is synonymous with "S. corporation" as defined in 15-30-101 and means a corporation for which a valid election under section 1362 of the Internal Revenue Code (26 U.S.C. 1362) is in effect.

(2) A corporation that would otherwise be a small business corporation may continue to be subject to the taxes imposed by Title 15, chapter 31, if all of the following conditions are met:

(a) on December 31, 1991, the corporation was doing business in Montana and had a valid subchapter S. corporation election but had not elected to be taxed as a Montana small business corporation;

(b) after December 31, 1991, the corporation has not filed as a Montana small business corporation; and

(c) the corporation files a corporate license tax return, as required by 15-31-111, reporting all income or loss as determined under Title 15, chapter 31, and attaches a copy of the federal subchapter S. corporate tax return.

History: En. 84-1501.1 by Sec. 1, Ch. 122, L. 1959; amd. Sec. 1, Ch. 405, L. 1977; R.C.M. 1947, 84-1501.1(a), (b); amd. Sec. 1, Ch. 667, L. 1983; amd. Sec. 1, Ch. 534, L. 1989; amd. Sec. 6, Ch. 807, L. 1991; amd. Sec. 13, Ch. 143, L. 2001; Sec. , MCA 1999; reds. by Sec. 16(2), Ch. 143, L. 2001.



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15-30-1102. Income or license tax involving pass-through entities -- information returns required. (1) Except as otherwise provided:

- (a) a partnership is not subject to taxes imposed in Title 15, chapter 30 or 31;
- (b) an S. corporation is not subject to the taxes imposed in Title 15, chapter 30 or 31; and
- (c) a disregarded entity is not subject to the taxes imposed in Title 15, chapter 30 or 31.

(2) Except as otherwise provided, each partner of a partnership described in subsection (1)(a), each shareholder of an S. corporation described in subsection (1)(b), and each partner, shareholder, manager, member, or other owner of an entity described in subsection (1)(c) is subject to the taxes provided in this chapter, if an individual, and to the taxes provided in Title 15, chapter 31, if a C. corporation.

(3) Income realized for federal income tax purposes by a financial institution that has elected to be treated as an S. corporation under subchapter S. of Chapter 1 of the Internal Revenue Code and by its shareholders that is attributable to the financial institution's change from the bad debt reserve method of accounting provided in section 585 of the Internal Revenue Code, 26 U.S.C. 585, is not taxable under Title 15, chapter 30 or 31, to the extent that the aggregate deductions allowed for federal income tax purposes under 26 U.S.C. 585 exceeded the aggregate deductions that the financial institution is allowed under 15-31-114(1)(b)(i).

(4) (a) A partnership that has Montana source income shall on or before the 15th day of the 4th month following the close of its annual accounting period file an information return on forms prescribed by the department and a copy of its federal partnership return. The return must include:

- (i) the name, address, and social security or federal identification number of each partner;
- (ii) the partnership's Montana source income;
- (iii) each partner's distributive share of Montana source income, gain, loss, deduction, or credit or item of income, gain, loss, deduction, or credit;
- (iv) each partner's distributive share of income, gain, loss, deduction, or credit or item of income, gain, loss, deduction, or credit from all sources; and
- (v) any other information the department prescribes.

(b) An S. corporation that has Montana source income shall on or before the 15th day of the 3rd month following the close of its annual accounting period file an information return on forms prescribed by the department and a copy of its federal S. corporation return. The return must include:

- (i) the name, address, and social security or federal identification number of each shareholder;
- (ii) the S. corporation's Montana source income and each shareholder's pro rata share of separately and nonseparately stated Montana source income, gain, loss, deduction, or credit or item of income, gain, loss, deduction, or credit;
- (iii) each shareholder's pro rata share of separately and nonseparately stated income, gain, loss, deduction, or credit or item of income, gain, loss, deduction, or credit from all sources; and
- (iv) any other information the department prescribes.

(c) A disregarded entity that has Montana source income shall furnish the information and file the returns the department prescribes. The return must include:

- (i) the name, address, and social security or federal identification number of each manager,

member, or other owner during the tax year;

(ii) the entity's Montana source income; and

(iii) any other information the department prescribes.

(d) (i) Except as provided in subsection (4)(d)(ii), a pass-through entity that fails to file an information return required by this section by the due date, including any extension, must be assessed a late filing penalty of \$10 multiplied by the number of the entity's partners, shareholders, managers, members, or other owners at the close of the tax year for each month or fraction of a month, not to exceed 5 months, that the entity fails to file the information return. The department may waive the penalty imposed by this subsection (4)(d)(i) as provided in 15-1-206.

(ii) The penalty imposed under subsection (4)(d)(i) may not be imposed on a pass-through entity that has 10 or fewer partners, shareholders, managers, members, or other owners each of whom:

(A) is an individual, an estate of a deceased individual, or a C. corporation;

(B) has filed any required return or other report with the department by the due date, including any extension of time, for the return or report; and

(C) has paid all taxes when due.

History: En. Sec. 11, Ch. 181, L. 1933; re-en. Sec. 2295.11, R.C.M. 1935; amd. Sec. 5, Ch. 260, L. 1955; amd. Sec. 4, Ch. 253, L. 1959; R.C.M. 1947, 84-4911; amd. Sec. 9, Ch. 143, L. 2001; Sec. , MCA 1999; redes. by Sec. 16(3), Ch. 143, L. 2001.



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15-30-1111. Taxation of partners, shareholders, managers, and members. (1) A partner of a partnership that has Montana source income and a resident who is a partner of a partnership during any part of the tax year shall, in computing net income, include the partner's distributive share of partnership income, gain, loss, deduction, or credit or item of income, gain, loss, deduction, or credit as determined pursuant to section 704 of the Internal Revenue Code (26 U.S.C. 704) and shall furnish a copy of the partner's federal schedule of the partner's share of income, deductions, and credits when filing the Montana tax return.

(2) A shareholder of an S. corporation that has Montana source income and a resident who is a shareholder of an S. corporation during any part of the tax year shall, in computing net income, include the shareholder's pro rata share of separately and nonseparately stated S. corporation income, loss, deduction, or credit as determined pursuant to sections 1366 and 1377 of the Internal Revenue Code (26 U.S.C. 1366 and 1377) and shall furnish a copy of the shareholder's federal schedule of the shareholder's share of income, deductions, and credits when filing the Montana tax return.

(3) A partner, shareholder, manager, member, or other owner of a disregarded entity that has Montana source income and a resident who is a partner, shareholder, manager, member, or other owner of a disregarded entity during any part of the tax year shall, in computing net income, include the disregarded entity's income, gain, loss, deduction, or credit or item of income, gain, loss, deduction, or credit.

History: En. Sec. 3, Ch. 143, L. 2001.



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15-30-1112. Composite returns and tax . (1) A partnership or S. corporation may elect to file a composite return and pay a composite tax on behalf of participants. A participant is a partner, shareholder, manager, or member who:

(a) is a nonresident individual whose only Montana source income for the tax year is from the entity and other partnerships or S. corporations electing to file the composite return and pay the composite tax on behalf of that partner, shareholder, manager, or member; and

(b) consents to be included in the filing.

(2) (a) Each participant's composite tax liability is the product obtained by:

(i) determining the tax that would be imposed, using the rates specified in 15-30-103, on the sum obtained by subtracting the allowable standard deduction for a single individual and one exemption allowance from the participant's share of the entity's income from all sources as determined for federal income tax purposes; and

(ii) multiplying that amount by the ratio of the entity's Montana source income to the entity's income from all sources for federal income tax purposes.

(b) A participant's share of the entity's income is the aggregate of the participant's share of the entity's income, gain, loss, or deduction or item of income, gain, loss, or deduction.

(3) The composite tax is the sum of each participant's composite tax liability.

(4) The electing entity:

(a) shall remit the composite tax to the department;

(b) must be responsible for any assessments of additional tax, penalties, and interest, which additional assessments must be based on the total liability reflected in the composite return;

(c) shall represent the participants in any appeals, claims for refund, hearing, or court proceeding in any matters relating to the filing of the composite return;

(d) shall make quarterly estimated tax payments as prescribed by 15-30-241 computed separately for each participant included in the filing of a composite return; and

(e) shall retain powers of attorney executed by each participant included in the composite return, authorizing the entity to file the composite return and to act on behalf of each participant.

(5) The composite return must be made on forms the department prescribes and filed on or before the due date, including extensions, for filing the entity information return. The composite return is in lieu of an individual income tax return required under 15-30-142 and 15-30-144.

(6) The composite tax is in lieu of the tax imposed under 15-30-103 and 15-30-105.

(7) The department may adopt rules that are necessary to implement and administer this section.

History: En. Sec. 4, Ch. 143, L. 2001.



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15-30-1112. Composite returns and tax . (1) A partnership or S. corporation may elect to file a composite return and pay a composite tax on behalf of participants. A participant is a partner, shareholder, manager, or member who:

(a) is a nonresident individual whose only Montana source income for the tax year is from the entity and other partnerships or S. corporations electing to file the composite return and pay the composite tax on behalf of that partner, shareholder, manager, or member; and

(b) consents to be included in the filing.

(2) (a) Each participant's composite tax liability is the product obtained by:

(i) determining the tax that would be imposed, using the rates specified in 15-30-103, on the sum obtained by subtracting the allowable standard deduction for a single individual and one exemption allowance from the participant's share of the entity's income from all sources as determined for federal income tax purposes; and

(ii) multiplying that amount by the ratio of the entity's Montana source income to the entity's income from all sources for federal income tax purposes.

(b) A participant's share of the entity's income is the aggregate of the participant's share of the entity's income, gain, loss, or deduction or item of income, gain, loss, or deduction.

(3) The composite tax is the sum of each participant's composite tax liability.

(4) The electing entity:

(a) shall remit the composite tax to the department;

(b) must be responsible for any assessments of additional tax, penalties, and interest, which additional assessments must be based on the total liability reflected in the composite return;

(c) shall represent the participants in any appeals, claims for refund, hearing, or court proceeding in any matters relating to the filing of the composite return;

(d) shall make quarterly estimated tax payments as prescribed by 15-30-241 computed separately for each participant included in the filing of a composite return; and

(e) shall retain powers of attorney executed by each participant included in the composite return, authorizing the entity to file the composite return and to act on behalf of each participant.

(5) The composite return must be made on forms the department prescribes and filed on or before the due date, including extensions, for filing the entity information return. The composite return is in lieu of an individual income tax return required under 15-30-142 and 15-30-144.

(6) The composite tax is in lieu of the tax imposed under 15-30-103 and 15-30-105.

(7) The department may adopt rules that are necessary to implement and administer this section.

History: En. Sec. 4, Ch. 143, L. 2001.



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15-30-1113. (Temporary) Consent or withholding -- notice. (1) A pass-through entity required to file an information return provided in 15-30-1102 that has a partner, shareholder, manager, member, or other owner who is a nonresident individual shall:

(a) on or before the due date, including extensions, for the information return:

(i) file a composite return with respect to the individual nonresident; or

(ii) file an agreement of the individual nonresident to:

(A) file a return in accordance with the provisions of 15-30-142;

(B) timely pay all taxes imposed with respect to income of the pass-through entity; and

(C) be subject to the personal jurisdiction of the state for the collection of income taxes and related interest, penalties, and fees imposed with respect to the income of the pass-through entity; and

(b) within the later of 180 days after the due date, including extensions, for the information return or the date the notice is sent as provided in subsection (2), remit an amount equal to the highest marginal tax rate in effect under 15-30-103 multiplied by the share of Montana source income reflected on the pass-through entity's information return of each nonresident individual for whom a composite return or agreement provided in subsection (1)(a) was not filed.

(2) As soon as practical, but not later than 60 days after the due date, including extensions, for the information return, the department shall send notice to the pass-through entity of the need to comply with subsection (1) and that the pass-through entity may be subject to penalties under 15-30-1102. If the department does not send notice, the pass-through entity is not subject to withholding.

(3) Any amount paid by a pass-through entity with respect to a nonresident individual pursuant to subsection (1)(b) must be considered as a payment on the account of the nonresident individual for the income tax imposed on the nonresident individual for the tax year pursuant to 15-30-105.

(4) A pass-through entity is entitled to recover a payment made pursuant to subsection (1)(b) from the partner, shareholder, manager, member, or other owner on whose behalf the payment was made.
(Effective January 1, 2003)

15-30-1113. (Effective January 1, 2003) . Consent or withholding. (1) A pass-through entity that is required to file an information return as provided in 15-30-1102 and that has a partner, shareholder, manager, member, or other owner who is a nonresident individual shall, on or before the due date, including extensions, for the information return:

(a) file a composite return with respect to the individual nonresident;

(b) file an agreement of the individual nonresident to:

(i) file a return in accordance with the provisions of 15-30-142;

(ii) timely pay all taxes imposed with respect to income of the pass-through entity; and

(iii) be subject to the personal jurisdiction of the state for the collection of income taxes and related interest, penalties, and fees imposed with respect to the income of the pass-through entity; or

(c) remit an amount equal to the highest marginal tax rate in effect under 15-30-103 multiplied by the nonresident individual's share of Montana source income reflected on the pass-through entity's information return.

(2) Any amount paid by a pass-through entity with respect to a nonresident individual pursuant to subsection (1)(c) must be considered as a payment on the account of the nonresident individual for

the income tax imposed on the nonresident individual for the tax year pursuant to 15-30-105.

(3) A pass-through entity is entitled to recover a payment made pursuant to subsection (1)(c) from the partner, shareholder, manager, member, or other owner on whose behalf the payment was made.

History: En. Secs. 5, 6, Ch. 143, L. 2001.



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15-30-1114. Review of pass-through entity taxation by department. (1) The department shall review, with the assistance of interested parties, the reporting and taxation of income that is flowing through pass-through entities and the method of reporting and taxation of this income in states other than Montana and shall consider recommendations concerning the methodology that Montana should use to ensure fair and equitable taxation of income that flows through pass-through entities to other entities.

(2) The department shall report to the revenue and transportation interim committee at least once each year on the findings and recommendations of the review conducted under subsection (1).

History: En. Sec. 15, Ch. 143, L. 2001.

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15-30-1121. Small business option unavailable on dissolution -- exception. In the case of corporation dissolution, no benefits may be taken under the "small business act" or under any law or regulation shifting the tax to be paid from the corporation to the shareholders unless all shareholders agree to assume personal income tax liability the same as they would bear if they were residents of this state.

History: En. Sec. 2, Ch. 60, L. 1963; R.C.M. 1947, 84-1501.3; Sec. , MCA 1999; redes. by Sec. 16(2), Ch. 143, L. 2001.

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For office use only

New York State Department of Taxation and Finance

IT-204-LL

Limited Liability Company/Partnership Filing Fee Payment Form

For calendar year 2001 or fiscal year beginning _____, 2001, and ending _____.

Print or type	Read the instructions below and on the back before completing this form.			Employer identification number
	Legal name			Change of business information
	Trade name of business if different from legal name above			<input type="checkbox"/> Check here if you have changed your mailing address and have not previously notified us (see instructions)
	Address (number and street or rural route)			Date business started
	City, village, or post office	State	ZIP code	Contact person's telephone number ()
	Principal business activity			

- 1 Did this entity have any income, gain, loss, or deduction derived from New York sources during the tax year? (see instructions) 1 ☐ Yes ☐ No

If No, skip lines 2 and 3. However, an authorized person must still sign the certification below. If Yes, continue with line 2.

- 2 Enter the total number of members or partners of this entity as of the last day of its tax year (see instructions) 2 ☐
- 3 LLC/LLP filing fee — Enter the amount from line 6 of the New York State filing fee worksheet in the instructions on the back (make check or money order for the full amount of the required filing fee payable to NYS LLC/LLP Fee; write your employer identification number and 2001 Filing Fee on the remittance and staple it to the top of this form) 3 ☐

Certification: I certify that all information contained on this form is true and correct to the best of my knowledge and belief.

Paid preparer's use only	Preparer's signature	▼ Preparer's SSN or PTIN	Sign here	Signature of general partner or member	Date
	Firm's name (or yours, if self-employed)	• Employer identification number			
	Address	Date		Mark "X" if self-employed <input type="checkbox"/>	

Instructions

General information

Chapter 576 of the Laws of 1994 allows for the formation of limited liability companies (LLCs) and limited liability partnerships (LLPs) in New York State (domestic LLCs or LLPs). In addition, recognition is given under New York State law for LLCs and LLPs formed under the laws of other states (foreign LLCs and LLPs).

Both domestic LLCs and LLPs are required to register with the New York State Department of State. In addition, foreign LLCs and LLPs that wish to carry on or conduct business or activities in New York State must also register with the Department of State. Taxpayers who have questions concerning the registration process should write to the New York State Department of State, 41 State Street, Albany NY 12231-0001, or call (518) 473-2492. Taxpayers who have questions concerning the New York tax treatment of LLCs and LLPs and payment of the filing fee should contact the Tax Department (see *Need help?* on the back page).

Effective August 8, 1995, certain investment companies that are established and regulated under Article 12 of the New York State Banking Law are able to organize themselves as limited liability investment companies (LLICs). The LLIC option is available only to Article 12 investment companies that serve as holding companies for foreign banking operations. Also, effective July 21, 1997, certain trust companies that are established and regulated under section 102-A of the New York State Banking Law are able to organize themselves as limited liability trust companies (LLTCs). The LLTC option is available only to Article 3 trust companies that do not receive deposits from the general public and are exempt from obtaining insurance of deposits and share accounts. Throughout these instructions, the term *limited liability company* includes a limited liability investment company and a limited liability trust company.

Instructions (continued)

New York tax treatment of LLCs and LLPs

An LLC or an LLP may be treated as a partnership or a corporation for federal income tax purposes. New York State law conforms to this federal treatment. Accordingly, an LLC or an LLP that is treated as a corporation for federal purposes must file a New York State corporation franchise tax return.

An LLC or an LLP that is treated as a partnership for federal purposes must, if it meets the requirements (see Form IT-204-I), file a New York State partnership return using Form IT-204, *Partnership Return*. Any LLC or LLP required to file Form IT-204 must also complete and file Form IT-204-LL. A single-member LLC is not treated as a partnership for federal purposes. Therefore, it is not subject to the filing fee and is not required to file Form IT-204 or Form IT-204-LL.

Filing fee

Every domestic or foreign LLC or LLP that is required to file a New York State partnership return and that has any income, gain, loss, or deduction from New York sources must pay a New York State filing fee. The amount of the filing fee is \$50 multiplied by the total number of members or partners in the LLC or LLP. However, the fee cannot be less than \$325 or more than \$10,000.

There is no proration of the filing fee if the LLC or LLP has a short tax year for federal tax purposes.

Who must file

This form must be filed by every limited liability company, limited liability investment company, limited liability trust company, or limited liability partnership that is required to file Form IT-204, *Partnership Return*. It is used as a means of remitting the state filing fee or to indicate why the LLC or LLP does not owe a fee for the current tax year.

When to file

An LLC or LLP that is not requesting an extension of time to file Form IT-204 must attach this form to the front of Form IT-204 when it is filed. For calendar year 2001, the filing deadline is April 15, 2002. If the partnership's principal business, office, or agency is located in the state of New York (except the city of New York and the counties of Nassau, Rockland, Suffolk, and Westchester), Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, or Vermont, the filing deadline is April 16, 2002. A full remittance of the filing fee due must be attached to the form and filed by the original due date of your return. If the LLC/LLP is requesting an extension of time to file, see *Extension* below.

Note: This form, together with Form IT-204, constitutes the complete partnership return. Failure to file either or both form(s) by the due date may result in the imposition of penalties for failure to timely file a partnership return.

Extension

An LLC or LLP that is requesting an extension of time to file Form IT-204 must complete and attach this form to the back of Form IT-370-PF, *Application for Automatic Extension of Time to File for Partnerships and Fiduciaries*. The LLC or LLP must include with the extension request a full remittance of any filing fee due. There is no extension of time for payment of the filing fee. If the LLC or LLP fails to pay the full amount of filing fee with its extension request, it must pay interest and a late payment penalty of $\frac{1}{2}\%$ per month, up to a maximum of 25% on the amount of fee not paid. **There is no extension of time to file Form IT-204-LL or to pay the annual fee.**

Line instructions

Name and address box — Enter the name, address, and identification number exactly as they appear or will appear on Form IT-204. Also enter the principal business activity, the date the business started, and the contact person's telephone number.

Change of business information — If you checked the box on the front, enter your new address in the space next to your preprinted address. You must report any changes in your business name, ID number, mailing address, physical address, telephone number, or owner/officer information on Form DTF-95, *Business Tax Account Update*. If only your address has changed, you may use Form DTF-96, *Report of Address Change for Business Tax Accounts*, to correct your address for this and all other tax types. You can get these forms by fax, phone, or from our Web site. See *Need help?* below for the phone number and Web address.

Line 1 — See *Income from New York State sources includes* under the heading **Who must file** on page 2 of Form IT-204-I, *Instructions for Form IT-204*, to determine if the LLC or LLP has any income, gain, loss, or deduction derived from New York sources during the tax year. **Note:** An LLC or LLP that has a net loss derived from New York sources during the tax year must still check the **Yes** box.

Line 2 — The total number of members or partners includes all resident and nonresident individuals, estates and trusts, and all corporations and

partnerships that were members or partners of the entity as of the last day of its tax year. This total may not necessarily agree with the number of partners entered at question **F** on Form IT-204.

Line 3 — New York State filing fee worksheet

1. Enter total number of members or partners from line 2 of Form IT-204-LL	1. _____
2. Multiply line 1 by \$50	2. _____
3. Maximum filing fee	3. \$10,000
4. Enter the smaller of line 2 or line 3	4. _____
5. Minimum filing fee	5. \$325
6. Enter the larger of line 4 or line 5 here and on Form IT-204-LL, line 3	6. _____

Full remittance of the amount shown on this line must accompany this form. Make your check or money order payable to **NYS LLC/LLP Fee**; write your employer identification number and **2001 Filing Fee** on the remittance and staple it to the front of this form.

Paid preparer must sign the return — Anyone you pay to prepare the return must sign it and fill in the other blanks in the paid preparer's area of the return. The preparer required to sign the return must sign it by hand; signature stamps or labels are not acceptable. If anyone prepares the return and does not charge you, the paid preparer's area should not be filled in.

Note to paid preparers — When signing a taxpayer's New York State income tax return, you must enter the same identification number that you used on the taxpayer's federal return, either your social security number or your federal preparer tax identification number (PTIN). If you did not prepare a federal income tax return for the taxpayer, you must use your PTIN if you have one; otherwise, use your social security number.

Paid preparers — Paid preparers may be subject to a penalty for failure to conform to certain requirements. For more information see the instructions for Form IT-204.

Where to file

If you have already filed Form IT-204 or Form IT-370-PF, mail Form IT-204-LL and your remittance, if any, to: **State Processing Center, PO Box 61000, Albany NY 12261-0001.**

Private delivery services

If you choose, you may use a private delivery service, instead of the U.S. Postal Service, to file your return. However, if, at a later date, you need to establish the date you filed your return, you cannot use the date recorded by a private delivery service **unless** you used a delivery service that has been designated by the U.S. Secretary of the Treasury or the Commissioner of Taxation and Finance. (Currently designated delivery services are listed in Publication 55, *Designated Private Delivery Services*. See *Need help?* below for information on ordering forms and publications.) If you use **any** private delivery service, whether it is a designated service or not, address your return to: **State Processing Center, 431C Broadway, Albany NY 12204-4836.**

Privacy notification

The Commissioner of Taxation and Finance may collect and maintain personal information pursuant to the New York State Tax Law, including but not limited to, sections 171, 171-a, 287, 308, 429, 475, 505, 697, 1096, 1142, and 1415 of that Law; and may require disclosure of social security numbers pursuant to 42 USC 405(c)(2)(C)(i).


This information will be used to determine and administer tax liabilities and, when authorized by law, for certain tax offset and exchange of tax information programs as well as for any other lawful purpose.


Information concerning quarterly wages paid to employees is provided to certain state agencies for purposes of fraud prevention, support enforcement, evaluation of the effectiveness of certain employment and training programs and other purposes authorized by law.

Failure to provide the required information may subject you to civil or criminal penalties, or both, under the Tax Law.

This information is maintained by the Director of the Registration and Data Services Bureau, NYS Tax Department, Building 8, Room 338, W A Harriman Campus, Albany NY 12227; telephone 1 800 225-5829. From areas outside the United States and Canada, call (518) 485-6800.

Need help?

 Tax information: 1 800 225-5829

 Forms and publications: 1 800 462-8100

Refund status: Access our Web site or call 1 800 443-3200;

if electronically filed: 1 800 353-0708;

direct deposit refunds: 1 800 321-3213

From outside the U.S. and outside Canada: (518) 485-6800

Fax-on-demand forms: 1 800 748-3676

Hearing and speech impaired (telecommunications device for the deaf (TDD) callers only): 1 800 634-2110



Internet access: www.tax.state.ny.us

Estimated tax: Access our Web site to check your balance and reconcile your account.